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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of)

Implementation of the Pay Telephone)
Reclassification and Compensation)
Provisions of the Telecommunications)
Act of 1996)

CC Docket No. 96-128

PETITION FOR RECONSIDERATION

THE CONSUMER-BUSINESS
COALITION FOR FAIR PAYPHONE-
800 FEES

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PETITION FOR RECONSIDERATION

The Consumer-Business Coalition for Fair Payphone-800 Fees (the “Consumer-Business Coalition”), by its attorneys and pursuant to 47 C.F.R. § 1.429, hereby requests that the Commission reconsider its decision in its Second Report and Order^{1/} in the above-captioned proceeding to require carriers to pay \$0.284 per call for all subscriber 800 and access code calls placed from payphones. The Commission’s action is inconsistent with the statute, which requires that payphone providers be *fairly* compensated for calls originating on their phones. Not only does the \$0.284 rate provide payphone owners with an unfair windfall, it has a severe and unwarranted impact on millions of consumer and business *users* of 800 service. Accordingly, the Commission should reconsider the rate it adopted in the Second Report and Order and instead require carriers to pay an incremental cost-based rate that, based on analyses already contained in the record, should be no more than \$0.06 per call.

^{1/} Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket No. 96-128, Second Report and Order, FCC 97-371 (rel. Oct. 9, 1997) (“Second Report and Order”).

INTRODUCTION AND SUMMARY

The Consumer-Business Coalition is comprised of a wide array of 800 service users significantly harmed by the Commission's decision to adopt an onerously high surcharge for 800 calls placed from payphones. The members of the coalition receive hundreds of millions of calls from payphones each year and are now facing steep increases in their already high costs of using 800 numbers. This rate increase could threaten the viability of smaller businesses dependent on 800 service and will cause ripple effects in the economy as a whole, as companies attempt to raise prices for other consumer goods and services or are forced to reduce the quality or variety of such items. In addition, organizations that have established 800-number hotlines to serve battered women, runaway children, and other persons in need of emergency assistance may have to reevaluate whether they can continue to provide these services. Because of the detrimental effects this new rate will have on small businesses, the Nation's economy, and the public interest, both the Consumer Federation of America and the International Communications Association have joined with the Consumer-Business Coalition to ask the Commission to reconsider its payphone compensation decision.

There is nothing in the Communications Act or its legislative history that compelled the result in the Second Report and Order. Indeed, Section 276 of the Act states only that payphone providers must be "fairly compensated" for calls made from their payphones. Granting payphone owners a windfall profit at the expense of long distance carriers and 800 service subscribers is entirely inconsistent with this fair compensation standard.

Moreover, given the lack of competition in the payphone market, the Commission's decision to rely on that market as a basis for rate setting departs radically from the Commission's own pronouncements on the value of cost-based pricing in such circumstances. For example,

throughout its proceeding aimed at opening the local exchange market to competition, the Commission repeatedly extolled the virtues of adopting cost-based rates to promote competition in a non-competitive marketplace. Here, in contrast, the Commission took exactly the opposite approach even though there is no evidence that the payphone market is any more competitive than the local telephone market. Significantly, in both circumstances, the Commission was implementing provisions of the Telecommunications Act of 1996, the express purpose of which is to “promote competition . . . in order to secure lower prices and higher quality services for American telecommunications consumers.”^{2/} That congressional objective will not be realized under the approach adopted in the Payphone Order.

Finally, there no basis for the Commission’s assumption that the payphone market will become sufficiently competitive in two years to warrant total deregulation of the rate paid for non-coin calls. Today, callers have virtually no choice in payphones at any particular location and there is no reason to believe that the market will undergo a complete metamorphosis by October, 1999. Moreover, even if point of sale competition were to eventually exist, most callers of 800 numbers have no incentive to seek out the least expensive payphone alternative because they do not pay for the call.

For these reasons, the Commission should reconsider its decision to use the coin rate as a surrogate for non-coin payphone calls, and should instead utilize a forward looking, incremental cost-based mechanism. The Commission should retain this rate cap until such a time as there is widespread point of sale competition in the payphone market.

^{2/} Pub. L. No. 104-104 (1996).

I. THE COMMISSION’S ADOPTION OF A \$0.284 PER-CALL COMPENSATION RATE SEVERELY HARMS 800 SERVICE SUBSCRIBERS AND ALL CONSUMERS

The Communications Act of 1934 states as its purpose the “[r]egulation of interstate and foreign communication by wire and radio so as to make available . . . to all people of the United States . . . a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at *reasonable charges* . . .”^{3/} In addition, Section 276 of the Act directs the Commission to ensure that payphone providers are *fairly compensated* and states among its goals “the widespread deployment of payphone services *to the benefit of the general public*.”^{4/}

The Commission’s implementation of Section 276 is fundamentally flawed because instead of providing for fair compensation to payphone owners, it grants them a windfall. In addition, the Commission ignored the public interest mandates of the Communications Act and the cost information contained in the record, and instead adopted a rate for 800 payphone calls based upon the deregulated local coin rate. In using this “market surrogate,” the Commission failed to take into account that the payphone market is not yet competitive on a point of sale basis and may never be. The Commission also did not address that, even if there were a choice of competing payphones, most 800 callers have no incentive to exercise discretion in their selection because they are not paying for the calls. Moreover, because it would jeopardize the business interests of many 800 service subscribers, the “alternative” of blocking 800 calls if the payphone provider fails to negotiate a lower charge is largely illusory.

The Commission’s failure to implement the statute in a reasonable manner has yielded a rate far in excess of that which would be present in a competitive market. As a result, payphone

^{3/} 47 U.S.C. § 151 (emphasis added).

providers will enjoy an enormous windfall, and 800 service subscribers and the public interest will be significantly harmed.

A. The Consumer-Business Coalition's Member Companies Will be Injured if the \$0.284 Rate is Sustained.

The Consumer-Business Coalition represents a group of 800 service users who are significantly harmed by the Commission's adoption of a cost-based rate. Its members are:

- American Trucking Associations -- the national trade association of the trucking industry, representing over 34,000 motor carriers of every type, including for-hire carriers, private carriers, truck leasing companies, owner-operators, and others. The trucking industry employs over nine million people nationwide and accounts for \$346 billion in annual revenue.
- Air Transport Association -- the principal trade and service organization representing twenty-one U.S. passenger and cargo airlines, and three foreign airlines; its member companies account for over 95 percent of all U.S. air passenger and cargo traffic. The air transport industry employs more than 564,000 employees and accounts for over \$85.5 billion in passenger and freight revenue each year.
- Consumer Federation of America -- a non-profit association of 240 pro-consumer groups, with a combined membership of 50 million, founded in 1968 to advance the consumer interest through advocacy and education.
- AAA -- a national membership organization, in business since 1902, that provides high quality automotive (including emergency roadside assistance), travel, financial, and insurance services to over 40 million members in the United States and Canada.
- National Network to End Domestic Violence -- a network of state domestic violence coalitions representing more than 2000 shelters and programs throughout the country.
- Truckload Carriers Conference-- the national trade association representing the irregular-route truckload segment of the motor carrier

^{4/}

47 U.S.C. § 276(b)(1) (emphasis added).

industry. Its member companies include more than 665 dry van, refrigerated, flatbed, and dump-trailer carriers.

- American Movers Conference -- the principal national trade association of the household goods moving industry, representing 2,600 member companies, including van lines, independent interstate carriers, and local agent moving companies.
- Transportation Intermediaries Association -- a national trade association representing over 700 member companies providing a wide variety of transportation-related services as property brokers, domestic freight forwarders, consolidators, ocean and air forwarders, intermodal marketing companies, perishable commodity brokers, and logistics management companies.
- International Taxicab and Livery Association -- the national organization of the owners and managers of taxicab and livery (limousine, executive sedan, airport shuttle, etc.) fleets, representing more than 900 fleets, which operate more than 75,000 passenger vehicles.
- American Airlines -- a wholly-owned subsidiary of AMR Corporation and one of the world's largest airlines.
- Nabisco, Inc. -- a consumer packaged goods company that markets, sells, and distributes its products to grocery stores throughout the United States and abroad.
- Virtual Voice Corporation -- a nationwide voice messaging service bureau serving customers in every state.
- International Communications Association -- the largest association of telecommunications users in the United States, with approximately 400 members who typically spend at least \$1 million per year for acquisitions of information and telecommunication services and equipment; its members collectively spend approximately \$32 billion annually for their information and telecommunication needs, and that number is growing.

As described in the declarations accompanying this petition, many of the Consumer-Business Coalition's member companies will suffer significant and unfair financial losses if the \$0.284 rate is not reduced to more appropriately reflect the costs of providing payphone service.

For example, the member companies of the American Trucking Associations, American Movers Conference, and the Truckload Carriers Association are especially vulnerable to the existence of a high per-call compensation rate because their drivers must call in from payphones -- often several times a day -- to coordinate dispatch, obtain directions, and communicate directly with operations facilities concerning customer demands, delivery schedules, vehicle safety or maintenance matters, accidents, and loading and unloading issues.^{5/} In addition to serving a general business purpose, some of these calls are necessary to comply with federal safety regulations.

The costs caused by the \$0.284 per-call compensation rate are significant for these companies. Schneider National, Inc., for instance, reports that its drivers make approximately 176,000 calls from payphones to the company's 800 number each month.^{6/} A \$0.284 surcharge on each of these calls will therefore cost Schneider an additional \$50,000 per month, or \$600,000 per year.^{7/} Similarly, J.B. Hunt Transport Services, Inc. indicates that its total monthly costs will increase by approximately \$210,000, or \$2.5 million each year, as a result of the surcharge.^{8/} UniGroup, Inc., the parent company of United Van Lines and Mayflower Transit, and C.R.

^{5/} See Declaration of Barry M. Riley (attached); Declaration of Eugene R. Dupré (attached); Declaration of John R. Pope (attached); Declaration of Cynthia M. Schaefer (attached); Declaration of Greg F. Atkinson (attached); Declaration of Daniel E. England (attached); Declaration of James H. McKinny (attached); Declaration of Pamela K. Guy (attached); Declaration of Donald J. Schneider (attached) (collectively referred to as "Trucking Company Declarations"). All declarations cited in this Petition are attached as Exhibit A and are arranged alphabetically by declarant's last name.

^{6/} Declaration of Donald J. Schneider.

^{7/} Id.

^{8/} Declaration of Pamela K. Guy.

England, Inc. report annual cost increases of \$825,000 and \$455,000, respectively.^{9/} Jet Express, Inc. states that its yearly telecommunications costs will triple – from \$84,000 to \$252,000 – draining its yearly net income by 16 percent.^{10/} Victory Express states that its annual 800-number costs will more than double – from \$336,645 to \$740,616 – corresponding to 12.8 percent of its net income.^{11/}

Other members of the Consumer-Business Coalition will also be adversely affected by the Commission's \$0.284 rate. For example, transportation-related companies such as property brokers, domestic freight forwarders, consolidators, intermodal marketing companies, ocean and air forwarders, and logistics management companies will face large cost hikes if the \$0.284 rate is not re-evaluated. A survey conducted by the Transportation Intermediaries Association ("TIA") reports that these companies receive on average over 48,000 800-number payphone calls each year.^{12/} TIA's 700 member companies alone will incur over \$9.6 million in added telecommunications charges as a result of the \$0.284 surcharge.^{13/}

The Nation's airlines will be especially hard hit by the high payphone rate. The Air Transport Association's member companies handle more than a billion passenger reservation calls each year, many of which originate from payphones. Passengers dial airline 800 numbers from payphones to check flight schedules, change reservations, make seat assignments, track lost

^{9/} Declaration of Brainerd W. LaTourette, Jr. (attached); Declaration of Daniel E. England.

^{10/} Declaration of Greg F. Atkinson.

^{11/} Declaration of Cynthia M. Schaefer. Other trucking companies will be similarly affected. See Declaration of Eugene R. Dupré (indicating a loss of 11 percent of its annual net income); Declaration of Barry M. Riley (4.5 percent); Declaration of John R. Pope (3.5 percent); Declaration of James H. McKinny (18 percent for the ten months ending October 1997).

^{12/} See Declaration of Robert A. Voltmann (attached).

^{13/} Id.

baggage, and manage their frequent flier member information. In addition, 800-number payphone calls are made by friends, business associates, and others (e.g., ground transportation companies, cargo companies) requiring such information, and flight crews frequently place 800 calls from payphones to obtain schedule information. Clearly, the impact of a \$0.284 per-call rate on these companies will be tremendous.

American Airlines echoes these concerns, noting that its customer service, both before and after flight, is dependent upon the availability of toll free calling. The airline estimates that 5 million of its 800-number inbound calls originate at payphones, which at \$0.284 each would result in an annual negative cost impact of approximately \$1.4 million.^{14/}

Nabisco, Inc., a consumer goods company and member of the Consumer-Business Coalition, reports that its sales force makes approximately 30,000 800-number payphone calls each day to enter orders, obtain route information and otherwise service its customers.^{15/} The imposition of a \$0.284 surcharge on these calls will add over \$2.1 million to the company's 800-number costs.^{16/} This 96 percent cost increase will severely hamper Nabisco's efforts to improve productivity and streamline its workforce. Roadside assistance club, AAA, similarly notes that with a significant portion of its 27 million annual emergency assistance calls coming from payphones each year, its costs will jump considerably.

Companies that use 800 numbers to fulfill their main business objectives are particularly vulnerable to telecommunications rate increases. For example, Virtual Voice, a voice messaging

^{14/} Declaration of David M. Rich (attached). American Airlines notes that because it has not historically tracked the number of its payphone calls, the impact could be much greater.

^{15/} Declaration of Orest R. Fiume (attached).

^{16/} Id.

company, reports that a \$0.284 surcharge will increase its costs in providing voice messaging service by 58 percent.^{17/} This places Virtual Voice in the untenable position of having to charge its customers considerably more than it has in the past, impeding it from effectively competing in the voice messaging service marketplace.^{18/} Virtual Voice predicts that the rate increase and the customer confusion created by the Commission's decision will cause significant customer attrition.^{19/} Other providers of voice mail and messaging services who have marketed their services on the basis of 800-number accessibility may be unable to survive this rate hike.

The Commission further failed to explain how it intends to protect businesses and consumers from exposure to fraud, the incentive for which is greatly enhanced by this excessive rate. As American Airlines calculates, continuous calls made from a single payphone to 800 numbers at one minute intervals would generate gross revenues of \$149,270 to the payphone owner annually. It would be extremely difficult and costly for a large user of toll free numbers to detect such activity and, given the large rewards, it would be an extremely lucrative enterprise for a "payphone provider."^{20/}

^{17/} Declaration of Monte A. Stern (attached).

^{18/} Id. The Commission's creation of such a high per-call surcharge has also created a myriad of logistical difficulties for Virtual Voice, which until now provided two toll-free 800 numbers for customers to access their voice mailboxes. Because of billing problems that were a direct result of the Commission's new surcharge, Virtual Voice has been forced to block, where possible, all calls to these numbers that originate from payphones. Virtual Voice has instead had to set-up two new 800 numbers for such calls; however, because access through these numbers triggers the company's software to add an automatic \$0.28 surcharge for such calls, customers wishing to avoid paying this surcharge must access the network through different numbers when dialing from non-payphones. This new system is likely to confuse the company's customers and will likely lead to significant customer attrition. Id.

^{19/} Id.

^{20/} See Declaration of David M. Rich. Other commenters previously raised this issue before the Commission. See, e.g., Reply Comments of Frontier Corporation (filed July 15, 1996) at 5-6

The Commission underestimated the adverse impact of its new payphone rate partially on the erroneous assumption that costs could be passed on to others, that 800-number users could “block” calls from certain payphones, or that subscribers would be able to negotiate better rates with interexchange carriers (“IXCs”). None of these mechanisms is sufficient to provide the relief to the businesses described above who have found themselves suddenly saddled with exorbitant new costs.

First, the Commission permitted IXCs to recover the cost of payments to payphone providers “from their customers,”^{21/} but 800 service subscribers – the “customers” in the Commission’s equation – usually have no way of recouping directly the charges that will be passed on to them by the IXCs. In the case of trucking companies, for example, the drivers placing 800-number calls from payphones are employees that cannot be charged for making such calls. Indeed, the reason the trucking companies use 800 service is to encourage their drivers to communicate frequently regarding delivery status, road conditions and the like.^{22/} Similarly, the airlines have established numerous 800 numbers so that consumers may make or change reservations, inquire about flight schedules, and purchase tickets from wherever they happen to be. Quite often, the airline does not have a direct customer relationship with the calling party and, even if it so desired, could not pass the payphone charge on to that party. Most businesses

(“With the high compensation rates that APCC and the BOCs propose, fraud is no less than invited by the compensation scheme”); Reply Comments of MobileMedia Communications, Inc. (filed July 15, 1996) at 7-8.

^{21/} Payphone Order at ¶¶ 17, 83; see also Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket No. 96-128, Order on Reconsideration, 11 FCC Rcd 21,233, ¶ 75 (1996) (“Order on Reconsideration”).

^{22/} See Trucking Company Declarations.

are in this same situation because, in general, the reason for providing an 800 number is to allow the end user to make a *toll-free* call.

Second, in defending its use of a market surrogate to set the coinless payphone rate, the Commission stated that IXC's and other users of subscriber 800 numbers can guard against incurring excessive per-call compensation charges by utilizing their ability to block calls from certain payphones.^{23/} This alleged bargaining chip is insignificant, however, because many IXC's and 800 number subscribers rely on the fact that their services may be accessed from *all* payphones. To make access available only from some locations would largely diminish the value of that company's service. Unless, as described below, there actually is widespread point of sale competition, blocking services from some or all payphones would be counterproductive and potentially fatal to a company's business prospects.

Finally, even if blocking were a viable alternative, IXC's and 800-number subscribers do not yet have the ability to block calls from all payphones even though the owners of these yet-to-be-coded payphones currently have the ability to assess the new surcharge.^{24/} In a recent order, the Commission waived until March 9, 1998, the requirement that local exchange carriers ("LECs") and payphone service providers implement payphone-specific coding digits to enable IXC's to track, and block, payphone calls as needed.^{25/} By weighing the balance of equities in favor of beginning per-call compensation before payphone-specific coding digits are in place for

^{23/} Payphone Order at ¶¶ 17, 49.

^{24/} See, e.g., Reply Comments of Paging Network, Inc. (filed Sept. 9, 1997) ("per-subscriber and per-call blocking, the foundation upon which the Commission's decision to adopt a market-based approach rests, is not possible.")

^{25/} Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket No. 96-128, Order, DA-2162 (rel. Oct. 7, 1997) ("Coding Digits Order") at ¶ 2.

all payphones, the Commission has effectively robbed IXC's and 800-number service providers of the one alleged recourse they have to paying per-call compensation.^{26/} Moreover, there is no guarantee that payphone-specific coding digits will in fact be in place for all payphones by March 9, 1998, as the Commission previously set the deadline for October 7, 1997, only to find that almost half of all payphones were not equipped to transmit payphone-specific coding digits by that date.^{27/}

As the foregoing demonstrates, 800 service subscribers will bear the brunt of the Commission's payphone compensation decision and will be unable to protect themselves adequately by cost pass-throughs or blocking. Nor are most 800 service subscribers in a position to negotiate with IXC's for lower payphone surcharges. Indeed, small businesses such as Catawba Rental Co., Inc. (a trucking company) and Virtual Voice are generally in a "take it or leave it" position because the volume of their 800 business is insufficient to warrant special deals. Even large users will likely be unable to convince IXC's – who themselves lack bargaining power with monopoly payphone providers – to lower the surcharge to cost. In light of the probably unanticipated effect the high surcharge will have on 800 service subscribers, and in the absence of any statutory compulsion to do otherwise, it is incumbent upon the Commission to designate a per-call compensation rate that is fair to all parties.

^{26/} Coding Digits Order at ¶ 13 ("[W]e conclude that the potential harm from the absence of compensation to [payphone service providers] would be greater than the potential harm to IXC's from the inability to block certain payphone calls before March 9, 1998.")

^{27/} Only sixty percent of all payphones were equipped to transmit payphone-specific coding digits by October 7, 1997. Id. at ¶ 12.

B. Selecting a Coin Rate Surrogate for Toll Free Per-Call Compensation is not in the Public Interest

The impact of the Commission's payphone rate extends beyond the business world and threatens both service organizations and the public interest as well. As the Commission has itself acknowledged, "[o]ne of the goals of Section 276 is the deployment of payphones to benefit the 'public health, safety and welfare.'"^{28/} In setting such a high per-call compensation rate, the Commission essentially ignored this congressional objective. For example, AAA's roadside assistance service receives approximately 27 million emergency calls each year, a significant portion of which are 800-number calls from payphones. If, as predicted by the Commission, the rate increase causes organizations such as AAA to block access to their twenty-four hour 800 numbers from some or all payphones, motorists will be left stranded, sometimes in the middle of the night, at isolated locations. While the Commission's premise is that widespread payphone competition may develop and prevent this dangerous result sometime in the future, as discussed below, no such competition exists now at any given emergency roadside location. Thus, the practical effect of the Commission's decision may be to keep current motorists stranded.

Similarly, many public service hotlines that assist runaways, drug addicts, victims of domestic violence, and psychologically troubled individuals will be adversely affected by the high surcharge for 800-number payphone calls. These organizations, which often are funded by the government and charities, cannot afford the steep increase in costs that the Commission's decision will engender. NNEDV, a network of state domestic violence coalitions, for instance, states that its national 800 hotline receives on average 8,000 calls per month.^{29/} Because many

^{28/} Payphone Order at ¶ 19 (citing 47 U.S.C. § 276(b)(1)).

^{29/} See Declaration of Donna F. Edwards (attached). Domestic violence hotlines using 800

battered women must leave their homes to seek safety or emergency medical assistance, it is likely that a fair number of those hotline calls originate at payphones. Indeed, the purpose of the domestic violence hotline is to encourage women who need help to call from any location and to do so with the expectation of confidentiality. NNEDV's ability to serve the needs of battered women will be severely compromised if it is forced either to curtail its hotline service or block access to its hotline from some or all payphones.^{30/}

C. The Record is Replete with Evidence that Small Businesses, End Users, and the Economy as a Whole Will Suffer as a Result of the Excessive Payphone Compensation Rate

Following the release of the Commission's Payphone Order, many companies filed letters with the Commission informing it of the adverse impact the adoption of a coin-based surrogate rate will have on their businesses.^{31/} For example, 1-800-FLOWERS stated that market forces are not sufficient "to set the rate at a competitive level or to bring to bear competitive forces,"

numbers are also operated by more than 25 state organizations. Id.

^{30/} The Commission should also recognize that its high per-call compensation rate will limit access to telephone service for low-income members of the public, many of whom rely on payphones and prepaid calling cards as their only source of telecommunications services. See generally Petition for Reconsideration of Consumers Union, et al. (filed Oct. 21, 1996); Reply Comments of International Telecard Ass'n (filed July 15, 1996).

^{31/} See Order on Reconsideration at ¶ 44 (citing Letter from Chris McCann, 1-800-FLOWERS, to Reed E. Hundt, Chairman, FCC, dated Oct. 21, 1996; Letter from John Lee, Budget Rent-A-Car Corp., to Regina Keeney, Chief, Common Carrier Bureau, dated Oct. 18, 1996); see also Letter from Elizabeth O'Hara, United Airlines, to Regina Keeney, Chief, Common Carrier Bureau, dated Oct. 18, 1996 (stating that a \$0.35 rate is significantly above the cost incurred for such calls); Letter from Hideo Hasui, Japan Airlines, to Regina Keeney, Chief, Common Carrier Bureau, dated Oct. 21, 1996 (recommending that the Commission adopt a lower per-call compensation rate or adopt a user-pays system); Letter from Thomas P. Jones, Jr., Access Health, Inc., to Regina Keeney, Chief, Common Carrier Bureau, dated Oct. 18, 1996 (same).

and that “[n]one of these developments will benefit consumers in the long run.”^{32/} Budget Rent-A-Car indicated that the new per-call compensation rate will likely result in an increase in Budget’s 800-number expenses of between “8 and 15 percent.”^{33/} Despite the record evidence that 800-number users would be significantly harmed if the Commission did not reduce the per-call compensation rate to cost, the Commission did little to acknowledge their concerns.

Further evidence of the impact this new surcharge will have on small businesses has been provided by the Commission itself. Whenever a federal agency issues a new regulation, it is obligated by law to prepare a regulatory flexibility analysis (“RFA”) which describes the impact the new regulation will have on small entities.^{34/} The purpose of preparing an RFA is to ensure that the regulatory agency is “tailor[ing] regulations to the size and resources of those who will be affected by them.”^{35/} In its initial Payphone Order RFA, the Commission stated that it did not have sufficient data to determine the number of small entity 800-number subscribers that would be affected by, among other things, its adoption of a high payphone surcharge. Instead, it concluded that, based on the fact that there were 6,987,063 800 numbers in use at the end of 1995, “fewer than 6,987,063 small entity 800-subscribers” would be affected by the new regulation.^{36/} When the Commission reduced the payphone rate from \$0.35 to \$0.284 in its

^{32/} Letter from Chris McCann, 1-800-FLOWERS, to Reed E. Hundt, Chairman, FCC, dated Oct. 21, 1996.

^{33/} Letter from John Lee, Budget Rent-A-Car Corp., to Regina Keeney, Chief, Common Carrier Bureau, dated Oct. 18, 1996.

^{34/} See 5 U.S.C. § 603.

^{35/} S. REP. NO. 95-1322 at 2 (1978).

^{36/} Payphone Order at ¶ 325.

Second Report and Order, it merely copied this same analysis *verbatim* and used it to describe the impact of its new rate.^{37/}

Despite the statutory mandate to do so, the Commission made no effort to determine how many small businesses would actually be affected by its decision, much less how the adverse impact of its regulation on such businesses could be lessened. This abdication of its obligation to consider the interests of small companies – and, in turn, the interests of all businesses and consumers – has resulted in an onerously high per-call compensation rate that, as described above, threatens the very viability of some businesses that rely on 800 number service. The Commission should therefore take the opportunity now to evaluate the impact of its decision on businesses and consumers and lower the 800-number per-call compensation rate to reflect the cost of providing payphone service.

II. THE COMMISSION’S ADOPTION OF THE \$0.284 RATE IS NOT COMPELLED BY THE STATUTE AND THE ASSUMPTIONS ON WHICH IT IS PREDICATED ARE FAULTY

The Commission was not led by any statutory compulsion to base its per-call compensation rate for subscriber 800 and access code calls on the deregulated local coin rate. To the contrary, Section 276 of the Act requires only that payphone owners be “*fairly compensated* for each and every completed intrastate and interstate call using their payphone.”^{38/} There were a number of approaches the Commission could have adopted to ensure fair compensation, many of which also would have “promoted the widespread deployment of payphone services to the benefit of the general public.”^{39/} Instead, the Commission chose to adopt a “market surrogate”

^{37/} See Second Report and Order at ¶ 148.

^{38/} 47 U.S.C. § 276(b)(1)(A) (emphasis added).

^{39/} 47 U.S.C. § 276 (b)(1).

derived from a market that enjoys virtually no competition. This decision represents a radical departure from prior Commission approaches to encouraging competition in non-competitive marketplaces and, as described above, harms businesses, consumers, and the public interest.

In the Payphone Order, the Commission embraced a market-based rate on the assumption that the payphone marketplace has the *potential* to become competitive.^{40/} The Commission itself acknowledged that competition in the payphone marketplace does not yet exist.^{41/} Many commenting parties echoed this sentiment after the Commission opted to establish a rate based on the local coin call price.^{42/} Although the payphone marketplace may theoretically become competitive in time, the Commission has presented no evidence of significant widespread competition at present to warrant reliance on market surrogates.^{43/}

In its various payphone-related orders, the Commission determined that a market surrogate is appropriate because multiple payphone service providers operate in many markets.^{44/}

^{40/} See Payphone Order at ¶¶ 11-12; see also Second Report and Order at ¶ 11. Ironically, the Commission decided to set a market-based rate on the assumption that the payphone marketplace will become competitive while at the same time recognizing that the payphone marketplace is not competitive and requires careful regulatory oversight to make it competitive.

^{41/} See Payphone Order at ¶ 8 (“Our *ultimate goal* is to have a competitive payphone industry that meets the needs of the public by a wide deployment of payphones. In our view, we can best facilitate this by putting in place rules and regulations that provide incentives to all the players in the industry to eliminate, as soon as possible, all of the market distorting factors that exist today”) (emphasis added).

^{42/} See, e.g., Comments of Competition Policy Institute at 3 (filed August 26, 1997) (arguing that a market-base rate is inappropriate because the payphone industry is not competitive, and because payphone service providers are monopolies or near monopolies); Reply Comments of PageMart at 7 (filed September 9, 1997).

^{43/} See Comments of Consumers Union at 4 (filed October 21, 1996) (“[T]he payphone marketplace is not competitive for the end user . . . End users have no choice, but to use the phone or drive or walk *to another location* which may not necessarily have cheaper rates.) (emphasis added).

^{44/} See, e.g., Second Report and Order at ¶ 95 (“[I]n the case of payphones, the presence of

While this might be true when viewing the payphone marketplace as a whole, there is no evidence that payphone competition is widespread on a point of sale basis.^{45/} Without this type of competition, whether or not multiple payphone service providers operate in many markets is irrelevant. Relying on the deregulated local coin rate will only be appropriate when end users are free to choose between competing payphone providers at the point of sale.

At many of the locations frequented by callers to the Consumer-Business Coalition's members there is only one payphone provider. For example, based upon the experience of many trucking companies, most truckstops generally provide exclusive access to just one payphone service provider.^{46/} The fact that there may be a competing payphone at a "nearby" location is irrelevant to these trucking companies. Few locations can accommodate 60 foot long, 80,000 pound trucks, and the costs of operating a large vehicle (especially fuel costs) make it economically impossible for drivers to search out alternative payphone locations.^{47/} In addition, because of federal restrictions on driving time and truck access, seeking a different payphone provider is generally infeasible.

Moreover, even if there were a real choice in payphone providers, many 800-number callers have no incentive to look for the least expensive payphone alternative. While a payphone

multiple [payphone service providers] already operating in many markets, and the structure of the industry that allows relatively easy entry and exit, leads us to conclude that we can rely on market forces to provide for efficient pricing of these services in the near future.")

^{45/} See, e.g., Petition for Reconsideration of Office of People's Counsel, District of Columbia ("OPC-DC") (filed October 21, 1996) at 8 ("The FCC's approach is premised on the assumption that competition is present today in this market. OPC-DC submits that this is not the case in any area in the United States.) OPC-DC also testified in other cases before the District of Columbia Public Service Commission that local payphones are competitive only to the extent that competition exists for locations, not for rates. Id.

^{46/} See Trucking Company Declarations.

user may forgo placing a coin call if the rate is too high, an 800-number caller, who is not paying the bill directly, will not exercise the same discretion. A person looking for flight schedule information, for instance, is unlikely to walk to the other side of an airport or hotel to use a different payphone. This absence of market discipline will leave 800-number subscribers in the position of having to pay for indiscriminate end-user conduct.

There is also no basis for the Commission's assumption that the payphone market will become competitive within two years. While allowing payphone owners to recoup supracompetitive profits may encourage additional entities to enter the business, there is no evidence that such rates will result in alternative providers at the point of sale. As MCI pointed out, in addition to creating a windfall for payphone service providers, non-cost based rates will be artificially driven up by location owners holding out for the highest bidding payphone provider.^{48/} Location owners, who often contract for the right to a percentage of the payphone provider's revenues, generally have no incentive to encourage payphone competition at their places of business. Smaller profits for payphone providers means smaller profits for location owners. Thus, rather than create widespread point of sale competition, the Commission's new regulations will lead to an unwarranted income transfer from consumers to payphone providers, and then from payphone providers to location owners.

Similarly, the Commission provided no support for its view that "the payphone marketplace has low entry and exit barriers," which will permit the payphone market to become competitive over time.^{49/} Even if establishing or expanding a payphone business were as easy as

^{47/} Id.

^{48/} Reply Comments of MCI at 10 (filed September 9, 1997).

^{49/} See Payphone Order at ¶ 70.

the Commission assumes,^{50/} most current payphone providers and new entrants will be unable to encroach upon the service territories of others when large fees are promised to location owners in exchange for exclusivity. Without point of sale competition, the number of payphones deployed or the number of new entrants in the market has no relevance to determining what the appropriate rate should be for coinless calls. Furthermore, even if competition on a location-by-location basis did develop, the “market” will not necessarily be able to set a fair rate for subscriber 800 payphone calls. As explained above, payphone providers are well aware that, because callers to toll free numbers are not footing the bill for the call, they generally have no reason to seek out the lowest cost payphone at any particular place of business.^{51/}

Rather than fulfill Congress’s objective of creating widespread payphone competition, setting a non-cost-based rate when there is virtually no point of sale competition in the payphone marketplace will have an anti-competitive effect and will prevent, or at least delay, true competition from emerging. In relying on market forces to set rates under these circumstances, the Commission has effectively enhanced the ability of incumbent payphone providers to use their revenues to protect their market share, as well as discourage potential competitors from entering the marketplace.^{52/} As AT&T pointed out, the \$0.35 per-call rate previously established

^{50/} The Payphone Order vaguely describes the payphone marketplace in two short paragraphs before concluding that if certain regulations are eliminated, the market has the potential to become competitive. See id. at ¶¶ 11-12.

^{51/} It is not clear whether the Commission envisioned that each member of Consumer-Business Coalition and all other 800 subscribers would install payphones throughout the country to avoid the new charges. Even if possible, this surely would be a cumbersome solution to the problems created by the Commission’s decision.

^{52/} This is especially true with respect to truckstops. Truckstops generate an extremely high volume of 800-number traffic, providing incumbent payphone service providers with significant funds to maintain their exclusivity at such locations. See Trucking Company Declarations.

by the Commission would permit payphone providers to recoup more than one billion dollars a year in compensation for subscriber 800 and access code calls.^{53/} By reducing this windfall only slightly, the Commission did nothing to address the problems faced by new payphone providers attempting to compete with entrenched incumbents for location contracts.

Although the Consumer-Business Coalition would agree that, whenever possible, market forces rather than regulation should be used to set prices, in this case reliance on the market has resulted in an arbitrary and artificially high rate. Because consumers have no meaningful choice of payphone providers at the point of sale, payphone owners are able to set coin call prices at levels far above the cost of providing the service. To then use that price as a basis for developing the coinless rate – which must be paid by captive 800 service subscribers – makes no sense. Accordingly, the Commission should set a cost-based rate for 800-number payphone calls and should retain that rate cap at least until widespread point of sale competition has developed in the payphone market.

III. THE COMMISSION SHOULD ADOPT A COST-BASED RATE FOR PER-CALL COMPENSATION

In determining carrier-to-carrier reciprocal compensation rates for local exchange competition, the Commission recognized the monopoly status of incumbent LECs and appropriately concluded that compensation should be determined on a cost basis. Specifically, the Commission stated that “[a]dopting a pricing methodology based on forward-looking, economic costs best replicates, to the extent possible, the conditions of a competitive market.”^{54/}

^{53/} Comments of AT&T (filed August 26, 1997); see also Reply Comments of International Telecard Ass’n (filed July 15, 1996) (“[E]xorbitant compensation rates . . . would yield excessive windfall profits for payphone providers.”)

^{54/} See Implementation of Local Competition Provisions in the Telecommunications Act of

The Commission also held that “a forward-looking cost methodology reduces the ability of an incumbent . . . to engage in anti-competitive behavior,” and that “[a]s a result of [pricing services] . . . at their economic cost, consumers will be able to reap the benefits of competition.”^{55/} Because, according to the Commission, a pricing methodology based on forward-looking incremental costs simulates the conditions in a competitive marketplace, new entrants may compete efficiently, which “should drive retail prices to their competitive levels.”^{56/}

The Commission’s decision in the payphone context to reject a cost-based rate in favor of a market-based approach rested on the assumption that, unlike the level of competition in the local exchange marketplace, the payphone marketplace is truly competitive.^{57/} Specifically, the Commission stated:

[T]he cost-based TELRIC [total element long run incremental cost] standard that the Commission relied upon in the local competition proceeding is inapplicable here because the payphone industry is not a bottleneck facility that is subject to regulation at virtually all levels Because the local exchange is not yet competitive, we could not rely on the market to set competitive rates for unbundled elements. In the case of payphones, the presence of multiple [payphone service providers] already operating in many markets, and the structure of the industry that allows relatively easy entry and exit, leads us to conclude that we can rely on market forces for efficient pricing of these services in the near future.^{58/}

1996, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15,499, ¶¶ 679, 620 (1996) (“Local Competition Order”) (“[B]ased on the current record, a cost-based pricing methodology based on forward-looking economic costs . . . is the approach for setting prices that best further the goals of the 1996 Act.”)

^{55/} Id.

^{56/} Id.

^{57/} Second Report and Order at ¶ 95.

^{58/} Id. at ¶¶ 94-95.